

Auditor-General of South Africa

Umzinyathi District Municipality

Audit report 2018-19

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on the Umzinyathi District Municipality

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of the Umzinyathi District Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2019, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. I do not express an opinion on the financial statements of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an opinion on these financial statements.

Basis for disclaimer of opinion

Infrastructure assets

3. The municipality did not recognise all items of infrastructure assets in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) GRAP 17, *Property, plant and equipment*. Completed assets were reported as one asset in the asset register and not componentised to allow each asset to be separately depreciated. In addition, as described in note 36 to the financial statements, the restatement was made to rectify a previous year misstatement, but it could not be substantiated by adequate supporting evidence. I was unable to confirm the restatement by alternative means.
4. Furthermore, we were unable to confirm the cost price of completed assets as well as work in progress additions, as the municipality was unable to provide payment vouchers which agree to the financial records, in support of the additions.
5. Consequently, I was unable to determine whether any further adjustments to infrastructure assets stated at R2,01 billion (2017-18: R1,80 billion) in note 8 to the financial statements was necessary.

Other reserves

6. I was unable to obtain sufficient appropriate audit evidence as the municipality did not have adequate internal controls to maintain records of accounts for other reserves. I was unable to confirm the other reserve by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to other reserves stated at R698,43 million in the statement of financial position.

Unspent conditional grant

7. I was unable to obtain sufficient appropriate audit evidence for unspent conditional grants of R303,99 million as the municipality did not have adequate record keeping systems. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to unspent conditional grants stated in note 15 to the financial statements.

General expenditure

8. I was unable to obtain sufficient appropriate audit evidence as the municipality did not have adequate internal controls to maintain records of transactions for general expenses. In addition, general expenses were not posted to the correct general ledger account. I was unable to confirm the general expenses by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to general expenditure stated at R151,29 million in note 35 to the financial statements.

Contingent liabilities

9. I was unable to obtain sufficient appropriate audit evidence for contingent liabilities, as the municipality did not maintain accurate and complete information due to the state of the accounting records, I could not confirm contingent liabilities by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to contingent liabilities of R90,42 million disclosed in note 42 to the financial statements.

Property, plant and equipment

10. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for property, plant and equipment. As described in note 36 to the financial statements, the restatement was made to rectify a previous year misstatement, but the misstatement could not be substantiated by supporting evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the property, plant and equipment corresponding figure stated at R105,97 million in note 10 to the financial statements.

Bad debts

11. I was unable to obtain sufficient appropriate audit evidence for bad debts written off due to the status of the accounting records. Consequently, I was unable to determine whether any further adjustments were necessary to bad debts stated at R93,64 million in note 32 to the financial statements.

Contracted services

12. I was unable to obtain sufficient appropriate audit evidence for payments made to contractors due to the status of the accounting records. Supporting documentation did not contain adequate information to determine whether all the expenditure was incurred.
13. Consequently, I was unable to determine whether any further adjustments were necessary to contracted services stated at R84,46 million (2017-18: R193,01 million) stated in note 34 to the financial statements.

Service charges

14. The municipality did not have adequate systems to maintain records of revenue from services charges. The detailed meter readings and invoices of consumers billed included negative billing of consumption and inconsistent readings.
15. In addition, I was unable to obtain sufficient appropriate audit evidence for transactions relating to receivables included in the general ledger. I could not confirm revenue from service charges and receivables balances by alternative means. The afore-mentioned had an impact on the receivables from exchange transactions, interest earned on debtors, debt impairment, payments received in advance and surplus for the period as well as on the accumulated surplus. Consequently, I was unable to determine whether any further adjustments were necessary to revenue from service charges stated at R62,42 million (2017-18: R59,36 million) in note 19; net receivables from exchange transactions stated at R57,16 million (2017-18: R66, 36 million) in note 6; interest earned on outstanding debtors stated at R18,77 million (2017-18: R14,12 million) in note 21 and payments received in advance stated at R14,54 million (2017-18: R2,20 million) in note 13 to the financial statements.

Trade payables and accruals

16. I was unable to obtain sufficient appropriate audit evidence for trade payables and accrued expenses due to the poor status of the accounting records. I could not confirm the trade payables and accrued expenses by alternative means. In addition, supporting documentation relating to the current year's trade payables and accrued expenses were not provided for audit.
17. Furthermore, included in trade payables and accrued expenses are goods and services received but not yet paid for. The municipality did not have adequate internal controls to maintain records of trade payables and accrued expenses for goods and services received. I was unable to obtain sufficient appropriate audit evidence to substantiate the trade payables and accrued expenses, as disclosed in note 13 to the financial statements.
18. The afore-mentioned had an impact on the general expenditure and surplus for the period as well as on the accumulated surplus. Consequently, I was unable to determine whether any further adjustments were necessary to accrued expenses stated at R59,37 million and trade payables stated at R37,40 million (2017-18: R67,08 million) in note 13 to the financial statements.

Water losses

19. I was unable to obtain sufficient appropriate audit evidence for water losses, as the municipality did not maintain accurate and complete records of the stock sheets used to determine water losses. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to water losses stated at R26,18 million as disclosed in note 51 to the financial statements.

Value-added tax (VAT) receivable

20. The municipality has not accounted for VAT on the accrual basis due to parameters of the system not been set to properly account for VAT transactions. I was unable to obtain sufficient appropriate audit evidence that VAT transactions for the current and previous year had been properly accounted for, due to the status of the accounting records. I was unable to confirm the VAT receivable balance by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to VAT receivables stated at R16,16 million (2017-18: R15,19 million) in note 5 to the financial statements.

Inventories

21. The municipality did not have adequate systems to maintain records of inventory transactions and journals processed on the system. There were no records of stock movements and stock counts that were performed during the year and at year end. I was unable to obtain sufficient appropriate audit evidence to confirm the inventory balance by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to inventory balance stated at R11,52 million in note 3 to the financial statements.

Cash flow statement

22. The municipality did not prepare the statement of cash flows in accordance with GRAP 2 *Cash Flow Statements*. Cash flows from operating activities were misstated as cash paid to suppliers were not correctly accounted for. Consequently, cash flows from operating activities was overstated by an amount of R176,24 million.

Other matter

23. I draw attention to the matter below.

Unaudited disclosure note

24. In terms of section 125(2)(e) of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

25. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and the Division of Revenue Act of South Africa, 2018 (Act No. 1 of 2018) (Dora), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

26. In preparing the financial statements, the accounting officer is responsible for assessing the Umzinyathi District Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

27. My responsibility is to conduct an audit of the financial statements in accordance with the International Standards on Auditing and to issue an auditor's report. However, because of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.
28. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and, parts 1 and 3 of the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (IESBA codes) as well as the ethical requirements that are relevant to my audit of the financial statements in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA codes.

Report on the audit of the annual performance report

Introduction and scope

29. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
30. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

31. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2019.

Development priorities	Pages in the annual performance report
KPA 2 – basic service delivery and infrastructure investment	xx – xx
KPA 3 – local economic development	xx – xx

32. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
33. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

Development priority 2 – basic service delivery and infrastructure investment

Various indicators

34. The reported targets in the annual performance report were not consistent with those approved in integrated development plan (IDP), as the IDP did not include the following targets:

Indicator description	Targets per IDP	Targets per annual performance report
No. of households to be provided with access to water within RDP Standards	None	2 500
No. of households provided with sanitation facilities	None	2 384
% of compliance to the quality standards for drinking water (SANS 241)	None	97%
% of compliance to the quality standards for the waste water treatment works	None	99%
Number of water treatment works operations and Maintenance undertaken	None	13
Number of waste water treatment works operations and Maintenance undertaken	None	48

Various indicators

35. I was unable to obtain sufficient appropriate audit evidence to support the reported achievement of the indicators listed below. This was due to a lack of proper performance management systems and processes and formal standard operating procedures that predetermined how the achievement would be measured, monitored and reported upon. I was unable to confirm the reported achievement of the indicators by alternative means. Consequently, I was unable to determine whether any adjustments were required to the achievement of the indicators below as reported in the annual performance report:

Indicator description	Reported achievement
% of compliance to the quality standards for drinking water (SANS 241)	95,4%
% of compliance to the quality standards for the waste water treatment works	35%
Number of water treatment works operations and maintenance undertaken	13
Number of waste water treatment works operations and maintenance undertaken	5

Various indicators

36. I was unable to obtain sufficient appropriate audit evidence for the related measures taken to improve performance as reported in the annual performance report for the indicators listed below. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance.

Indicator description	Planned targets	Reported achievement
No. of households to be provided with access to water within RDP Standards	2 500	240
No. of households provided with sanitation facilities	2 384	1 890
% of compliance to the quality standards for drinking water (SANS 241)	99.0%	95,4%
% of compliance to the quality standards for the waste water treatment works	97%	35%

Development priority 3 – local economic development

Various indicators

37. The reported targets in the annual performance report were not consistent with those approved in IDP, as the IDP did not include the following targets:

Indicator description	Targets per IDP	Reported achievement
Number of agricultural Co-operatives supported with mechanisation, enterprise development and market support	None	7
No of SMME's in the manufacturing sector supported with mechanisation, enterprise development and market support	None	0
No of farmer production support Units (FPSU) supported with mechanisation and input	None	2
Number of tourism structures supported with grant	None	4
No. of tourism events to advertise Umzinyathi as the destination of choice	None	2
No. of jobs created through Municipality's LED initiatives	None	96
Number of jobs opportunities created through EPWP	None	331

Various indicators

38. I was unable to obtain sufficient appropriate audit evidence for the related measures taken to improve performance as reported in the annual performance report for the indicators listed below. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance.

Indicator description	Planned targets	Reported achievement
Number of agricultural Co-operatives supported with mechanisation, enterprise development and market support	10	7
No. of SMME's in the manufacturing sector supported with mechanisation, enterprise development and market support	2	0
No. of tourism events to advertise Umzinyathi as the destination of choice	6	2
No. of jobs created through Municipality's LED initiatives	225	96
Number of jobs opportunities created through EPWP	2 607	331

Other matters

39. I draw attention to the matters below.

Achievement of planned targets

40. The annual performance report on pages xx to xx includes information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 34 to 38 of this report.

Adjustment of material misstatements

41. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of development priority 2 - basic service delivery and infrastructure investment. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

42. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
43. The material findings on compliance with specific matters in key legislations are as follows:

Financial statements

44. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets and disclosure notes identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a disclaimer audit opinion.

Expenditure management

45. Money owed by the municipality was not always paid within 30 days or within an agreed period from the date of receipt of the invoices, as required by section 65(2)(e) of the MFMA.
46. Reasonable steps were not taken to prevent irregular expenditure of R355,66 million as disclosed in note 45 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by the non-compliance with supply of chain management regulations.
47. Reasonable steps were not taken to prevent unauthorised expenditure of R67,70 million, as disclosed in the statement of comparison of budget information and actual information, as required by section 62(1)(d) of the MFMA.

Revenue management

48. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

Asset management

49. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Consequence management

50. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
51. Irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

Strategic planning and performance

52. The service delivery and budget implementation plan for the year under review did not include the service delivery targets and performance indicators for each quarter, as required by section 1 of the MFMA.

Conditional grants

53. Performance in respect of programmes funded by the Water Services Infrastructure Grant and Regional Bulk Infrastructure Grant were not evaluated, as required by section 12(5) of Dora.

Procurement and contract management

54. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements. This was due to poor records management. A similar limitation was also reported in the prior year.
55. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for the required minimum period of days, as required by regulations 22(1) and 22(2) of the Municipal Supply Chain Management Regulations of 2005 (GNR. 868 dated 30 May 2005 (MSCMR)).
56. In some instances, goods and services of a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of the regulation 17(a) and (c). MSCMR. Similar non-compliance was also reported in the prior year.
57. Awards were made to providers who were in the service of other state institutions or whose directors were in the service of other state institutions, in contravention of section 112(j) of the MFMA and regulation 44 of the MSCMR.
58. In some instances, sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by inviting competitive bids and that deviations approved by the accounting officer were only if it was impractical to invite competitive bids, as required by regulations 19(a) and 36(1) of the MSCMR. Similar non-compliances were also reported upon in the previous year.

59. In some instances, the bid documentation for procuring commodities designated for local production and content, did not stipulate the minimum threshold for local production and content as required by regulation 8(2) of the preferential procurement regulations of 2017 (GNR. 40553 dated 20 January 2017) (PPR).

60. In some instances, contracts were extended or modified without the approval of a properly delegated official, in contravention of regulation 5 of the MSCMR.

Human resource management

61. I was unable to obtain sufficient appropriate audit evidence to confirm that a senior manager, who was previously dismissed for financial misconduct, was re-appointed before the expiry of the stipulated 10 years' term, as required by section 57A (3) of the MSA.

62. Appointments were made in posts which were not provided for in the approved staff establishment, as required by section 66(3) of the MSA.

Other information

63. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the mayor's foreword and executive summary; governance as well as appendices that include recommendations by the municipal audit committee.

The other information does not include the financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in this auditor's report.

64. As a result of the disclaimer of opinion expressed on the financial statements, I do not conclude on material misstatements of the other information relating to the financial statements. If, based on the work I have performed relating to the audit of performance information and compliance with legislation, I conclude that there is a material misstatement of this other information, I am required to report that fact.

65. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

66. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the disclaimer of opinion, the findings on the performance report and the findings on compliance with legislation included in this report.

67. Leadership, management as well as oversight did not respond adequately and with the required urgency to our repeated messages on addressing the prior years' audit findings (action plan), mitigating risks and improving the internal control environment. Our messages and the delivery thereof have been consistent for a number of years, but the slow response to this is standing in the way of improvements in audit outcomes and this is exacerbated by the lack of effective consequence management.
68. Management did not ensure that monthly information was reconciled for infrastructure assets, revenue and receivables as well as inventory to ensure the quality of monthly management information and ultimately the year-end financial statements.
69. Management did not adequately monitor and review the performance information to ensure that it was well defined and agreed with supporting documentation.
70. The low level of action in response to the high levels of non-compliance, poor audit outcomes, SCM transgressions and unauthorised, irregular as well as fruitless and wasteful expenditure demonstrate a lack of consequences in the municipality for poor performance and transgressions.
71. Record and safe-keeping of files, documents as well as portfolio of evidence for both financial, compliance as well as performance information was not at the desired standards.

Other reports

72. I draw attention to the following engagements conducted by various parties that had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

Investigations

73. An investigation was conducted by an independent consulting firm, on behalf of the Department of Cooperative Governance and Traditional Affairs. The investigation covered the period 1 July 2015 to 30 June 2017 and related to expenditure for boreholes and debt collection that was not supported by adequate documentary evidence. The final report was tabled to council after year-end.

74. An investigation covering the period 1 July 2014 to 30 June 2018 is being conducted by an independent consulting firm at the request of the municipality. The firm is looking into value for money on expenditure and whether supply chain processes were followed relating to the construction of the municipality's disaster management centre. The investigation was finalised in the current year and the final report was tabled to council after year end.

Auditor General

Pietermaritzburg

30 November 2019



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in this auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Umzinyathi District Municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease continuing as a going concern
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.

